

Message Text

CONFIDENTIAL

PAGE 01 ROME 11128 01 OF 02 150038Z

60/53

ACTION EUR-25

INFO OCT-01 EA-11 ISO-00 SP-03 AID-20 EB-11 NSC-07 RSC-01

CIEP-03 SS-20 STR-08 OMB-01 CEA-02 L-03 H-03 PA-04

PRS-01 USIA-15 CIAE-00 COME-00 FRB-03 INR-11 NSAE-00

XMB-07 OPIC-12 LAB-06 SIL-01 DRC-01 (ISO) W

----- 073528

P R 141025Z AUG 74

FM AMEMBASSY ROME

TO SECSTATE WASHDC PRIORITY 6420

INFO DEPARTMENT OF TREASURY WASHDC PRIORITY

AMEMBASSY BERN

AMEMBASSY BONN

AMEMBASSY BRUSSELS

USMISSION EC BRUSSELS

AMEMBASSY THE HAGUE

AMEMBASSY LONDON

AMCONSUL MILAN

AMCONSUL NAPLES

AMEMBASSY OTTAWA

AMEMBASSY PARIS

USMISSION OECD PARIS

AMEMBASSY STOCKHOLM

AMEMBASSY TOKYO

C O N F I D E N T I A L SECTION 1 OF 2 ROME 11128

C O R R E C T E D C O P Y (FOR ADDEES)

E.O. 11652: GDS

TAGS: EFIN, ECON, IT

SUBJECT: STATUS REPORT ON ITALIAN FINANCIAL AND ECONOMIC SITUATION

REF: ROME A-523 OF AUGUST 9

1. SUMMARY. ALTHOUGH ITALIAN FINANCIAL SITUATION
CONTINUES TO BE WORRISOME, PARTICULARLY WITH REGARD TO BALANCE OF
CONFIDENTIAL

CONFIDENTIAL

PAGE 02 ROME 11128 01 OF 02 150038Z

PAYMENTS DEFICIT, BUDGET DEFICIT AND

INFLATION, REAL GROWTH AND EMPLOYMENT SITUATION FOR 1974 LOOK FAIRLY SATISFACTORY. PARLIAMENT COMPLETED RATIFICATION OF FISCAL PACKAGE ON AUGUST 13 AND RESTRICTIVE MONETARY POLICY IS STILL BEING PURSUED. SOME DOWNTURN IN GROWTH AND EMPLOYMENT IS STILL EXPECTED IN COMING MONTHS, BUT EMBASSY DOES NOT FORESEE REALLY SHARP DROP IN GROWTH RATE NOR CRITICAL RISE IN UNEMPLOYMENT BEFORE END-1974. END SUMMARY.

2. GROWTH; EMPLOYMENT; BUSINESS OUTLOOK. SUCH STATISTICAL EVIDENCE AS IS AVAILABLE CONTINUES TO POINT TO RELATIVELY SATISFACTORY RATE OF REAL GROWTH OF GNP THIS YEAR. RECENT IMF REPORT ON ECONOMIC SITUATION PREPARED IN CONNECTION WITH CONSULTATIONS ON STANDBY FORECASTS REAL GNP GROWTH IN 1974 OF ABOUT 4 PERCENT. EMBASSY IS INCLINED TO THINK THAT GROWTH MAY BE SOMEWHAT HIGHER THAN THAT. IN FIRST QUARTER OF 1974, AGRICULTURAL PRODUCTION INDEX WAS UP 3.5 PERCENT OVER SAME PERIOD OF 1973. (IN SAME PERIOD OF 1973 AGRICULTURAL PRODUCTION HAD BEEN DOWN SLIGHTLY FROM 1972.) IN FIRST SIX MONTHS OF THIS YEAR INDUSTRIAL PRODUCTION INDEX ROSE 12.1 PERCENT COMPARED TO SAME PERIOD OF 1973. THIS EXCEPTIONALLY HIGH RATE REFLECTED LOW 1973 BASE DUE TO STRIKES IN FIRST FOUR MONTHS OF THAT YEAR. HOWEVER, MAY AND JUNE 1974 INCREASES OVER SAME MONTHS OF 1973 WERE EACH UP ABOUT 6 PERCENT. UNEMPLOYMENT IN APRIL WAS 484 THOUSAND COMPARED TO 735 THOUSAND IN SAME MONTH OF 1973, I.E., SHOWING REDUCTION OF MORE THAN ONE-THIRD. (EMBASSY BELIEVES THAT FEARS OF 1 MILLION UNEMPLOYED IN AUTUMN ARE EXAGGERATED.) LATEST ISCO SURVEY OF BUSINESS OPINION DOES INDICATE SIGNIFICANTLY MORE PESSIMISTIC GENERAL VIEW OF SITUATION IN COMING MONTHS AS REGARDS ORDERS, PRODUCTION AND GENERAL LEVEL OF ECONOMIC ACTIVITY. ON OTHER HAND, FOREIGN ORDERS SEEM TO BE HOLDING UP AND BUSINESS EXPECTATIONS RE PRICE INCREASES ARE SOMEWHAT LESS PESSIMISTIC THAN EARLIER.

3. BALANCE OF PAYMENTS. BALANCE OF PAYMENTS DEFICIT CONTINUES TO BE SERIOUS PROBLEM WITH CUMULATIVE DEFICIT (ADJUSTED FOR COMPENSATORY EUROMARKET BORROWING) OF \$6.3 BILLION THROUGH JULY. HOWEVER, STATISTICS FOR JULY SHOWED BALANCE OF PAYMENTS SURPLUS OF \$393 MILLION. IMPROVEMENT WAS SOMEWHAT SURPRISING SINCE UNDERLYING DEFICIT, ESPECIALLY TRADE DEFICIT, COULD NOT HAVE DISAPPEARED OVERNIGHT. TIMING OF IMPROVEMENT IMMEDIATELY FOLLOWING G-10 AGREEMENT ON POSSIBLE USE OF CENTRAL BANK GOLD AS COLLATERAL FOR FOREIGN LOANS

CONFIDENTIAL

PAGE 03 ROME 11128 01 OF 02 150038Z

AND FOLLOWING WITHDRAWAL OF RUMOR GOVERNMENT'S RESIGNATION SUGGESTS IMPORTANCE OF PSYCHOLOGICAL FACTORS BEHIND B/P IMPROVEMENT IN JULY. OTHER PROBABLY FACTORS WERE REVERSAL OF LEADS AND LAGS ON TRADE, REPATRIATION OF ITALIAN CAPITAL, SOME REDUCTION IN TRADE DEFICIT, SEASONAL STRENGTH FROM TOURISM AND FOREIGN FINANCING OF PRIOR IMPORT DEPOSIT. EFFECTS OF TIGHT CREDIT WERE ALSO IMPORTANT. ALTHOUGH NO STATISTICS AVAILABLE FOR AUGUST, WE UNDERSTAND THAT THROUGH AUGUST 13 BOI HAS ONCE AGAIN HAD NET SALES OF FOREIGN EXCHANGE TO SUPPORT

LIRA. THIS MAY REFLECT ADVERSE EFFECT OF RECENT OUTBREAK OF VIOLENCE (E.G., ATTACK ON ROME-BRENNER TRAIN).

4. FOR FIRST HALF OF YEAR, TRADE DEFICIT (IMPORTS C.I.F.) WAS ABOUT \$6.2 BILLION, OF WHICH NET PETROLEUM DEFICIT WAS ABOUT \$3.5 BILLION. LATTER FIGURE COMPARES WITH PETROLEUM DEFICIT OF \$1.0 BILLION IN SAME PERIOD OF 1973. DATA ON AVERAGE CHANGES IN VOLUME OF EXPORTS AND IMPORTS (CUSTOMS DATA) THROUGH FIRST FOUR MONTHS OF THIS YEAR SHOW RELATIVE IMPROVEMENT WITH VOLUME OF IMPORTS (C.I.F.) UP ONLY 9.5 PERCENT, WHILE EXPORTS ROSE BY 26.3 PERCENT. SAME AVERAGE MONTHLY FIGURES FOR CY 1973 WERE 13.5 PERCENT FOR IMPORTS AND 4.2 PERCENT FOR EXPORTS. HEART OF PROBLEM REMAINS SHARPLY WORSENERED TERMS OF TRADE. THUS, IN FIRST FOUR MONTHS OF 1974 MONTHLY AVERAGE INCREASE IN IMPORT PRICES COMPARED TO SAME PERIOD OF 1973 WAS 80.7 PERCENT, WHILE EXPORT PRICES ROSE BY 34.8 PERCENT.

5. EVEN IF IMPROVEMENT IN TRADE AND BALANCE OF PAYMENTS DEFICITS SHOULD CONTINUE, THERE WILL STILL BE SERIOUS FINANCING PROBLEM FOR REMAINDER OF 1974 AND 1975, IN LARGE PART DUE TO OIL DEFICIT. IMF STAFF STILL FORECASTING CURRENT ACCOUNT DEFICIT FOR 1974 OF ABOUT \$10 BILLION AND DEFICIT IN 1975 OF PERHAPS \$5 BILLION. IN EARLY AUGUST ITALY MADE GOLD TRANCHE AND FIRST CREDIT TRANCHE DRAWING OF \$623 MILLION FROM IMF. ADDITIONAL \$900 MILLION IS STILL AVAILABLE UNDER STANDBY AND ITALY MAY BE ABLE TO MAKE INITIAL DRAWING OF PERHAPS \$300 MILLION FROM NEW IMF OIL FACILITY. PROSPECTS FOR ADDITIONAL MEDIUM - AND LONG-TERM EUROLOANS DO NOT APPEAR BRIGHT AT PRESENT BECAUSE OF GENERAL UNCERTAINTY IN MARKET AND BECAUSE OF LARGE EXPOSURE OF EUROBANKS VIS-A-VIS ITALY. HOWEVER, IF BALANCE OF PAYMENTS BEGINS TO SHOW STEADY IMPROVEMENT, ITALIAN CREDIT RATING COULD IMPROVE IN COMING MONTHS. ALTHOUGH FURTHER SHORT-TERM FINANCING IS AVAILABLE IN FORM OF CENTRAL BANK SWAPS, ITALIAN

CONFIDENTIAL

NNN

CONFIDENTIAL POSS DUPE

PAGE 01 ROME 11128 02 OF 02 141337Z

53

ACTION EUR-25

INFO OCT-01 EA-11 ISO-00 L-03 H-03 PA-04 PRS-01 USIA-15

SP-03 AID-20 EB-11 NSC-07 RSC-01 CIEP-03 SS-20 STR-08

OMB-01 CEA-02 CIAE-00 COME-00 FRB-03 INR-11 NSAE-00

XMB-07 OPIC-12 LAB-06 SIL-01 DRC-01 /180 W

----- 065675

P R 141025Z AUG 74
FM AMEMBASSY ROME
TO SECSTATE WASHDC PRIORITY 6421
INFO DEPARTMENT OF TREASURY WASHDC PRIORITY
AMEMBASSY BERN
AMEMBASSY BONN
AMEMBASSY BRUSSELS
USMISSION EC BRUSSELS
AMEMBASSY THE HAGUE
AMEMBASSY LONDON
AMCONSUL MILAN
AMCONSUL NAPLES
AMEMBASSY PARIS
USMISSION OECD PARIS
AMEMBASSY STOCKHOLM
AMEMBASSY TOKYO

C O N F I D E N T I A L SECTION 2 OF 2 ROME 11128

MONETARY AUTHORITIES STILL ANTICIPATE
NEED FOR LONGER TERM FINANCING, NOT ONLY TO DEAL WITH REMAINING
DEFICIT IN 1974 BUT ALSO WITH CONTINUING DEFICIT EXPECTED IN 1975.

6. WEAKENING OF LIRA THIS MONTH HAS RESULTED IN ITS DEPRECIATING
VERY NEARLY TO RECORD LOW. LATTER OCCURRED ON JUNE 12 WHEN BOI
WEIGHTED AVERAGE INDEX SHOWED DEPRECIATION OF 18.80 PERCENT FROM
FEBRUARY 1973 SECOND DOLLAR DEVALUATION. ON AUGUST 13 LIRA DEP-
CIATION WAS 18.51 PERCENT.

7. MONETARY POLICY. PROVISIONAL BOI DATA THROUGH JUNE SHOW THAT
CONFIDENTIAL
CONFIDENTIAL

PAGE 02 ROME 11128 02 OF 02 141337Z

DOMESTIC CREDIT EXPANSION IN APRIL-JUNE QUARTER OF ABOUT 5,753
BILLION WAS WITHIN QUARTERLY STANDBY CEILING OF 6,000 BILLION LIRE.
INTEREST RATES REMAIN HIGH IN NOMINAL TERMS, ALTHOUGH SOMEWHAT
LOWER THAN FEW WEEKS AGO AND NOT HIGH IN REAL TERMS WHEN ADJUSTED
BY CURRENT RATE OF INFLATION. PRIME RATE IS NOW AROUND 18-20 PERCENT
,
48-HOUR INTERBANK RATE ABOUT 17-1/2 PERCENT AND THREE-MONTH
INTERBANK RATE ABOUT 18-3/4 PERCENT. ALTHOUGH SHORT-TERM RATES
HAVE RECEDED SOMEWHAT, LONGER TERM RATES SEEM TO BE RISING. THIS IS
PARTLY BECAUSE BANK OF ITALY IS NO LONGER INTERVENING AS HEAVILY IN
SUPPORT OF FIXED-INTEREST SECURITIES AND BECAUSE SOME SAVINGS
BANKS WHICH FORMERLY INTERVENED TO SUPPORT PRICE OF THEIR MORTGAGE
CERTIFICATES HAVE CEASED TO DO SO. MONETARY AUTHORITIES CONTINUE
TO GIVE HIGH PRIORITY TO CREDIT TIGHTNESS, EVEN OVER BALANCE OF
PAYMENTS FINANCING, AS EVIDENCED BY RECENT BOI DECISION TO
FREEZE LEVEL OF SHORT-TERM FOREIGN BORROWING BY COMMERCIAL BANKS AT
JULY 19 LEVEL.

8. FISCAL POLICY. GOVERNMENT AND PARLIAMENT HAVE CONCENTRATED

THEIR ATTENTION IN RECENT WEEKS ON RATIFICATION OF JULY DECREE LAWS CONTAINING TAX INCREASES. ALTHOUGH NUMEROUS AMENDMENTS WERE MADE IN DECREES, SOME OF THESE CHANGES HAVE INCREASED ANTICIPATED REVENUES AND OTHERS DECREASED IT. GOVERNMENT INSISTS THAT 3,000 BILLION LIRE TOTAL REVENUE FROM TAX AND PUBLIC UTILITY RATE INCREASES WILL BE PRESERVED. FULL IMPACT OF 3,000 BILLION LIRE PACKAGE WILL ONLY BE FELT OVER TIME, SINCE SOME TAX MEASURES CALL FOR IMMEDIATE PAYMENTS BUT OTHERS FOR PERIODIC PAYMENTS. THERE IS, OF COURSE, ROOM FOR DOUBT ABOUT ACCURACY OF REVENUE FORECASTS AND ABOUT ABILITY TO COLLECT SOME OF NEW TAXES.

9. PROVISIONAL BOI DATA ON FINANCING OF CASH BUDGET DEFICIT THROUGH FIRST HALF OF 1974 (USING DEFINITION AGREED TO WITH IMF) SHOW TOTAL CREDIT OF 3,959 BILLION LIRE, AGAINST SEPARATE IMF FINANCING CEILING OF 4,600 BILLION FOR FIRST HALF OF CY 1974. (CEILING FOR CALENDAR YEAR IS 9,200 BILLION LIRE.)

10. PRICES AND WAGES. PRICES CONTINUE TO RISE AT RAPID RATE, WITHOUT ANY CLEAR PATTERN WHEN DISCOUNTED FOR PETROLEUM PRICE INCREASES. BOTH RETAIL PRICE INDEX AND COST-OF-LIVING INDEX IN JULY WERE UP ABOUT 19 PERCENT OVER SAME MONTH OF 1973. AVERAGE MONTHLY INCREASE IN TWO INDICES THROUGH JULY WAS 1.8 PERCENT EACH, OR
CONFIDENTIAL
CONFIDENTIAL

PAGE 03 ROME 11128 02 OF 02 141337Z

INCREASE AT ANNUAL RATE OF ALMOST 22 PERCENT. (EXCLUDING EFFECT OF MARCH AND JULY PETROLEUM PRODUCT PRICE INCREASES, AVERAGE MONTHLY COST OF LIVING INCREASE WAS 1.5 PERCENT, OR ANNUAL RATE OF 18 PERCENT.) AVERAGE MONTHLY WHOLESALE PRICE INCREASE THROUGH JUNE WAS 3.8 PERCENT, ALTHOUGH RATE OF INCREASE IN SECOND QUARTER WAS SIGNIFICANTLY LOWER THAN IN FIRST QUARTER. FURTHER PRICE INCREASES CAN BE EXPECTED IN COMING MONTHS AS RESULT OF DECISION TO RAISE PUBLIC UTILITY RATES AND TO TERMINATE MOST OF (RATHER INEFFECTIVE) PRICE CONTROLS WHICH HAD BEEN INTRODUCED IN MID-1973. ON OTHER HAND, REDUCED RATE OF INCREASE IN WORLD COMMODITY PRICES SHOULD BEGIN TO BE FELT AT RETAIL LEVEL.

1. NOTWITHSTANDING COMPLAINTS FROM LABOR UNIONS ABOUT PRICE INFLATION, AVAILABLE STATISTICS SHOW THAT WAGE INCREASES ARE KEEPING UP WITH OR EXCEEDING PRICE INCREASES. IN MAY 1974 MINIMUM CONTRACTUAL WAGE RATES (INCLUDING FAMILY ALLOWANCES) FOR WORKERS HAD RISEN 23.0 PERCENT IN INDUSTRY AND 34.8 PERCENT IN COMMERCE, WHILE RATES FOR SALARIED EMPLOYEES WERE UP 18.1 PERCENT AND 30.0 PERCENT, RESPECTIVELY. PERSISTENT EXCESS OF WAGE RATE INCREASES OVER PRODUCTIVITY GAINS AND OVER PRICE RISES CANNOT HELP BUT CONTRIBUTE TO INFLATIONARY PRESSURES.

12. COMMENT. AT MID-AUGUST ITALIAN ECONOMIC AND FINANCIAL SITUATION CONTINUES TO BE SERIOUS BUT NOT OF CRISIS PROPORTIONS. REAL GROWTH FOR CY 1974 SHOULD BE FAIRLY SATISFACTORY AND EXPECTED DROP IN EMPLOYMENT DUE TO DOWNTURN IN ECONOMIC ACTIVITY LATE IN 1974, IN EMBASSY OPINION, SHOULD BE TOLERABLE.

SIZE OF BALANCE OF PAYMENTS DEFICIT THIS YEAR AND EXPECTED
CONTINUATION OF DEFICIT IN 1975 PRESENTS SERIOUS FINANCING PROBLEM
WHICH WILL HAVE TO BE MET FROM VARIETY OF SOURCES. DEVALUATION OF
LIRA SEEMS TO BE HAVING FAVORABLE EFFECT IN ENCOURAGING EXPORTS
AND DISCOURAGING IMPORTS, BUT WORSENERD TERMS OF TRADE ARE STILL
OER-RIDING. MONETARY POLICY CONTINUES TIGHT, ALTHOUGH REAL INTEREST
RATES ARE NOT HIGH. CASH BUDGET DEFICIT TO DATE HAS BEEN LOWER THAN
EXPECTED BUT IS STILL A LONG-TERM PROBLEM. GOI HAS BEEN ABLE TO
PUSH THROUGH ITS TAX PROGRAM IN PARLIAMENT APPARENTLY WITHOUT
SERIOUS EROSION IN EXPECTED REVENUES. PRICE RISES ARE STILL
EXCEPTIONALLY HIGH ALTHOUGH, IN PART, THEY REFLECT DELIBERATE POLICY
OF PERMITTING PRICE INCREASES (E.G. GASOLINE) TO DISCOURAGE CONSUMER
DEMAND. VOLPE

CONFIDENTIAL

NNN

Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: ECONOMIC CONDITIONS, ECONOMIC REPORTS
Control Number: n/a
Copy: SINGLE
Draft Date: 14 AUG 1974
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: golinofr
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1974ROME11128
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: GS
Errors: N/A
Film Number: D740223-1114
From: ROME
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1974/newtext/t19740848/aaaabouj.tel
Line Count: 289
Locator: TEXT ON-LINE, ON MICROFILM
Office: ACTION EUR
Original Classification: CONFIDENTIAL
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 6
Previous Channel Indicators:
Previous Classification: CONFIDENTIAL
Previous Handling Restrictions: n/a
Reference: ROME A-523 OF AUGUST 9
Review Action: RELEASED, APPROVED
Review Authority: golinofr
Review Comment: n/a
Review Content Flags:
Review Date: 03 APR 2002
Review Event:
Review Exemptions: n/a
Review History: RELEASED <03 APR 2002 by shawdg>; APPROVED <26 JUN 2002 by golinofr>
Review Markings:

Declassified/Released
US Department of State
EO Systematic Review
30 JUN 2005

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: STATUS REPORT ON ITALIAN FINANCIAL AND ECONOMIC SITUATION
TAGS: EFIN, ECON, IT
To: STATE
Type: TE
Markings: Declassified/Released US Department of State EO Systematic Review 30 JUN 2005